

Welcome to Understanding the Impact of FAR Part 31.2 Cost Principals on Indirect Rates

*Presented by: Gelman, Rosenberg & Freedman CPAs,
Aldebaron, Inc. (SYMPAQ) and
Government Contract Compliance Management, LLC*

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Webinar Objectives

Learning Objective

To provide attendees with a better understanding the Impact of FAR Part 31.2
Cost Principals on Indirect Rates

Instructional Delivery Methods

Group Internet-based

Recommended CPE

1.5 CPE Credit

Recommended Fields of Study

Accounting

Prerequisites

None required

Advance Preparation

None

Program Level

Basic

Course Registration Requirements

None

Refund Policy

No fee is required to participate in this session.

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Understanding the Impact of FAR Part 31.2 Cost Principals on Indirect Rates

GovCon Webinar Series: Part 4 of 5

April 2, 2019

Presenters

Featured Guest Speaker

Moderator

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Meet Your Instructors



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Polling Question #1

What is your knowledge level of the FAR Part 31.2 cost principles for government contractors?

- a. 25%
- b. 50%
- c. 75% or more
- d. *I am new to this*

The background of the slide is a blurred photograph of a library. It shows rows of bookshelves filled with books, receding into the distance. Several light bulbs are hanging from the ceiling, some in sharp focus and others blurred, creating a bokeh effect. The overall lighting is warm and soft.

FAR Part 31.2

Cost Principles

FAR 31.201-2 Allowability

- Criteria for determining allowability
 - FAR Part 31 Cost Principles
 - Allocability
 - Reasonableness
 - Cost Accounting Standards (CAS)
 - Specific terms and conditions of the contract



FAR 31.201-2 Allowability

Continued

- Selected Cost Principles (Far 31.205.xx)
 - Specific allowability criteria for over 52 items with 6 principles removed/reserved
- An Express for Unallowable Costs: FAR 31.001 Definitions
 - Costs which by law, regulation, or clause specifically named and stated to be unallowable



What could possibly go wrong?



Allocation Bases

Unallowable Costs

- **Must separate Unallowable Costs**
 - Including Direct Unallowable Costs
 - **Unallowable direct costs remain direct costs** and remain part of any appropriate allocation base for computing applicable rates
 - Unallowable direct costs ARE NOT Overhead or G&A
 - Unallowable indirect costs are not necessarily G&A costs
 - Use of G/L accounts to record expressly unallowable costs

Expressly Unallowable Costs

- Penalties for claiming EXPRESSLY unallowable costs
 - Up to 300%
 - Limited to costs that are specifically unallowable per FAR 31.2



Expressly Unallowable Costs

Continued

- **Objective Standard:** For a cost to be expressly unallowable the Government must show that it was unreasonable under all circumstances for a person in the contractor's position to conclude that the costs were allowable
 1. A cost principle states in direct terms that the costs are unallowable, or leaves little room for differences of opinion, AND
 2. The cost principle identifies the specific cost or type of costs in a way that leaves little room for interpretation

MRD 14-PAC-022(R) and cases cited therein

Raytheon Co., ASBCA No. 57742, 2017 WL 1740026 (Apr. 17, 2017)

Exelis Inc., ASBCA No. 58966, 2017 WL 1355015 (Mar. 29, 2017)

Not “Objective” Principles

- Unreasonable
- Not allocable
- Not IAW terms of the contract
- Subjective criteria (e.g. “...practice followed so consistently as to imply...”)
- Requires application of criteria beyond the cost principle (e.g. IRC, CAS, etc.)
- No direct statement and does not provide allowability criteria

DCAA List

MRD 14-PAC-021(R)

- Listed costs include
 - Executive compensation in excess of the statutory limit
 - Certain advertising
 - Bad debts
 - Interest
 - Excess rent over allowable costs incurred by related party
 - Contributions
 - Entertainment & alcoholic beverages
 - Employee morale – holiday parties, tickets



FAR 31.201-6(a)/(b)

Directly Associated Cost

- Any cost which is generated solely as a result of another cost, which would have not been incurred had the other cost not be incurred
- Directly associated cost applies to unallowables
- Not only is legal costs relating to the collection of bad debts unallowable, but also corporate's involvement in terms of labor, fringe, overhead

FAR 31.201-5

Credits

- Applicable portion of any income, rebate, allowance or other credit to any allowable cost will be credited to the government via the expense account as a cost reduction or a cash refund
- Example: gain on the sale of an asset

FAR 31.201-4

Allocability

- Definition: Allocability is a cost that is assignable or chargeable to one or more contracts on the basis of the relative benefits received
- Incurred specifically for a contract
- Benefits both the contract and other work, can be distributed in a reasonable proportion to the benefits received
- Necessary to the overall operation of the business, though no direct relationship to a particular contract

FAR 31.201-2

Reasonableness

- Definition: Reasonable is when in its nature and amount, it does not exceed what a prudent person in the conduct of competitive business (i.e. arm's length transaction)
- No presumption of reasonableness
- The government can challenge a cost as unreasonable
- Contractor has the burden of proof

FAR 31.201-2

Contract Terms

- Specific contract clauses may restrict the allowability or recoverability of certain costs
- Not To Exceed limitations on travel or material
- Burden rate ceilings
- Limits on the amount of overtime premium
- Pre-contract costs
- Reduction of fixed fee based on level of effort

Other FAR Issues

- Documentation
- Contractor must maintain and retain the necessary documentation to support costs or the government can disallow them
- FAR 52.215-2(f) Retain 3yrs after final payment
- Total Cost Definition FAR 31.201-1
- The sum of direct and indirect costs allocable to a contract less credits, refunds, rebates; plus the cost of money; and excluding unallowable costs

A hand holding a pen is writing on a checklist on a grid-lined notebook. The checklist has several items with checkboxes, some of which are already checked. The background is a light blue gradient.

FAR Part 31-205 Individual Cost Principles

Master List

Allowability Of Selected Costs Under *FAR 31.205*

Selected Costs May Be Allowable (A), Unallowable (UA), or Allowable With Restrictions (AWR)

- Alcoholic Beverages [31.205-51](#) (UA)
- Asset Valuations Resulting from Business Combinations [31.205-52](#) (AWR)
- Bad Debts [31.205-3](#) (UA)
- Bonding Costs [31.205-4](#) (A)
- Compensation for Personal Services [31.205-6](#) (A)(UA)(AWR)
- Contingencies [31.205-7](#) (A)(UA)
- Contributions or Donations [31.205-8](#) (UA)
- Cost of Money [31.205-10](#) (AWR)
- Research & Development Costs [31.205-48](#) (UA)(AWR)
- Depreciation [31.205-11](#) (AWR)
- Economic Planning Costs [31.205-12](#) (A)(UA)
- Employee Morale, Health, Welfare, Food Service, & Dormitory Costs & Credits [31.205-13](#) (A)(AWR)
- Entertainment Costs [31.205-14](#) (UA)
- Fines, Penalties, & Mischarging Costs [31.205-15](#) (UA)(AWR)
- Gains & Losses on Disposition or Impairment of Depreciable Property or Other Capital Assets [31.205-16](#) (AWR)

Allowability Of Selected Costs Under FAR 31.205

Continued

Selected Costs May Be Allowable (A), Unallowable (UA), or Allowable With Restrictions (AWR)

- Goodwill [31.205-49](#) (UA)
- Idle Facilities & Idle Capacity Costs [31.205-17](#) (UA)(AWR)
- Independent Research & Development/Bid & Proposal Costs [31.205-18](#) (UA)(AWR)
- Insurance & Indemnification [31.205-19](#) (A)(UA)(AWR)
- Interest & Other Financial Costs [31.205-20](#) (UA)(AWR)
- Labor Relations Costs [31.205-21](#) (A)
- Legal & Other Proceedings Costs [31.205-47](#) (UA)(AWR)
- Lobbying and Political Activity Costs [31.205-22](#) (UA)
- Losses on Other Contracts [31.205-23](#) (UA)
- Manufacturing & Production Engineering Costs [31.205-25](#) (A)
- Material Costs [31.205-26](#) (A)
- Organization Costs [31.205-27](#) (UA)
- Other Business Expenses [31.205-28](#) (A)
- Plant Protection Costs [31.205-29](#) (A)
- Patent Costs [31.205-30](#) (A)(UA)(AWR)

Allowability Of Selected Costs Under FAR 31.205

Continued

Selected Costs May Be Allowable (A), Unallowable (UA), or Allowable With Restrictions (AWR)

- Plant Reconversion Costs [31.205-31](#) (UA)(AWR)
- Pre-contract Costs [31.205-32](#) (AWR)
- Professional & Consultant Service Costs [31.205-33](#) (A)(UA)(AWR)
- Public Relations & Advertising Costs [31.205-1](#) (UA)(AWR)
- Recruitment Costs [31.205-34](#) (A)(UA)(AWR)
- Relocation Costs [31.205-35](#) (A)(UA)(AWR)
- Rental Costs [31.205-36](#) (A)(AWR)
- Royalties & Other Costs for Use of Patents [31.205-37](#) (AWR)
- Selling Costs [31.205-38](#) (A)(UA)
- Service & Warranty Costs [31.205-39](#) (A)
- Special Tooling & Special Test Equipment Costs [31.205-40](#) (AWR)
- Taxes [31.205-41](#) (A)(UA)
- Termination Costs [31.205-42](#) (A)(AWR)
- Trade, Business, Technical, and Professional Activity Costs [31.205-43](#) (A)(AWR)
- Training & Education Costs [31.205-44](#) (A)(UA)(AWR)
- Travel Costs [31.205-46](#) (AWR)

FAR 31.205-1

Advertising & P/R

Unallowable advertising

- Promote sale of products or services
- Conventions, exhibits, free goods, samples, magazines, newspapers, trade papers, web sites, direct mail, dealer cards, window displays, radio, and television
- In-house salaries, travel associated with advertising or P/R is unallowable



FAR 31.205-1

Advertising & P/R Cost



Unallowable Public Relations (PR) costs

- Maintaining, protecting and enhancing the image of a concern or its products
- Favorable relations with the public at large or a particular segment of the population

FAR 31.205-3

Bad Debts Expense

- Write-offs to bad debts expense whether estimated or actual are unallowable
- Directly associated costs for legal or collection agency is unallowable

FAR 31.205-4

Bonding Costs

- Bonding costs are required when the Government requires assurance against financial loss to itself or others by reason of the act of default of the contractor. This may include the contractor's requirement to assure itself against financial loss.
- Costs of bonding pursuant to the terms of the contract are allowable
- Costs of bonding required by contractor in their general business are allowable to the extent in accordance with sound business practices, rates and premiums are reasonable in the circumstances
- Types of bonds: bid, performance, payment, advance payment, infringement and fidelity bonds

FAR 31.205-6

Compensation for Personal Services

- Definition-Compensation
- Criteria for allowability
 - Performed in current year
 - Not retroactive payments to prior years
 - Total compensation must be reasonable
 - Specific elements of compensation may be restricted
 - Conform to company's policies or be so consistently followed to imply a practice

FAR 31.205-6

Compensation for Personal Services (continued)

- Changes or new plans to compensation requires
 - No presumption of allowability for changes or new items of compensation
 - Notify ACO before implementation or within reasonable time period after start up
 - Afford the government time to review changes or new items to the compensation plan

FAR 31.205-6

Compensation for Personal Services (continued)

- Reasonableness test
 - At the individual component level (e.g. bonus) or at the total level of compensation
- Basis of reasonableness (benchmarking)
- Similar position
- Similar size company
- Similar type of industry (SIC codes)
- Same geographic region
- DCAA maintains their own database and salary surveys
- DCAA can challenge initial review of facts
 - Any element of compensation (e.g. 401(k) plan)
 - The total compensation level as being out of line

FAR 31.205-6

Compensation for Personal Services (continued)

- Reasonableness test
- No presumption of allowability, contractor has the burden of proof
- Offsets to disallowance are permitted: DCAM 6-413.7
 - Between employees within same job level for allowable items
 - Limited to: wages and salaries, bonuses, deferred compensation, pension and savings plan benefits, health and life insurance, and paid absences
- Differentials or COLAs
 - Additional cost due to the payment of higher income taxes when working abroad, or hazards in a foreign country allowable, payment of any domestic income taxes are **unallowable**

FAR 31.205-6

Compensation

- **Bonuses & Severance**
 - Written formal plan between employer-employee or consistently followed to imply practice to ensure **allowability**
- **Back Pay: retroactive adjustment of prior year's wages is **unallowable****
 - Resulting from negotiated settlement or court order for underpayments is **allowable** if underpaid work actually performed
- **Stock Options, stock appreciation rights, phantom stock plans, junior stock conversions and dividends are **unallowable****
 - Compensation based on changes in stock price

FAR 31.205-6

Compensation (continued)

- Pension
 - Costs in current year not funded by tax return filing or extension are **not allowable** in subsequent years
 - For nonqualified pension plans on a pay-as-you-go basis to be **allowable** in the current year, the pension cost shall be allocated in the cost accounting period that the pension costs are assigned
- Pension payments must be disbursed pursuant to an agreement between contractor and employees before work or services are performed in accordance with established plan to be **allowable**
 - The cost of changes in pension plans are **not allowable** if the changes are discriminatory to the Government or not applied consistently for all employees under similar circumstances in the future
- Excess assets from defined benefit plan revert to contractor, surplus is credited to the appropriate indirect accounts

FAR 31.205-6

Compensation (continued)

- Fringe benefits
- Employee rebate and purchase discount plans granted to employees on products and services purchased by the contractor or affiliates are **unallowable**
- Allowable: paid absences, insurance and unemployment plans
- Personal use of *company-owned/fringe benefits* autos is unallowable per FAR 31.205-6(m)(2)

FAR 31.205-6

Compensation (continued)

Compensation Cap Amounts for Contracts Awarded on or after June 24, 2014¹

For Costs Incurred	Cap Amount ¹
1/1/2018 - 12/31/2018	\$525,000 ²
1/1/2017 - 12/31/2017	\$512,000 ³
1/1/2016 - 12/31/2016	\$500,000 ⁴
6/24/2014 - 12/31/2015	\$487,000

¹ Current FY Cap Amount = Prior FY Cap Amount x Change in Employment Cost Index for all workers [i.e., BLS Table 4. Compensation (Not Seasonally Adjusted) Employment Cost Index for total compensation, for civilian workers, by occupational group and industry. (Twelve Months Ended September 30)]. Source:

<https://www.bls.gov/web/eci/ecicois.pdf>

² 2018: \$512,000 x (130.7/127.5), rounded to the nearest thousand

³ 2017: \$500,000 x (127.5/124.6), rounded to the nearest thousand

⁴ 2016: \$487,000 x (124.6/121.4), rounded to the nearest thousand

Polling Question #2

What is the Cost of Money?

- a. *Interest*
- b. *Unrecovered asset cost due to write-downs*
- c. *Implicit interest return on fixed assets*
- d. *Implicit interest return on leased assets*
- e. *I don't know*

FAR 31.205-7

Contingencies

- **Unallowable** for historical cost purposes, incurred and recorded on books
- Future estimates, two kinds of contingencies
 - Allowable when arising out presently known and existing conditions such as the anticipated costs for materials rejects and defective work
 - Unallowable since cannot measure so precisely to provide equitable results to contractor or Government. Example: the results of pending litigation excluded from cost estimates

FAR 31.205-8

Contributions or Donations

- Contributions or donations are **unallowable**



FAR 31.205-10

Cost of Money

- Cost of money is the imputed cost of interest on borrowings pertaining to plant and equipment
 - It is an incurred cost for cost reimbursement purposes under Cost type contracts and progress payments under Fixed type contracts
 - Schedule F and F-1 of DCAA ICE model
 - Cost of money is **allowable** provided it is measured, assigned and allocated per CAS 414 and/or CAS 417
 - For it to be **allowable** on a contract, the estimated cost of money must be identified and included in the proposal for a particular contract

FAR 31.205-11

Depreciation

- Depreciation is permitted (**allowable**) on plant, equipment and other capital facilities subject to the following
 - Only residual values that exceed 10% may be used in establishing depreciable costs
 - Full CAS-covered contractors must comply with CAS 409 – Depreciation of Tangible Capital Assets or contractors can make an election to follow CAS 409 and then are obligated to comply with CAS 409 hence forth
 - For contractors not required to comply with CAS 409, **allowable** depreciation shall not exceed the amount used for financial statement purposes and consistent treatment of depreciation in the same manner as other non-Federal business

FAR 31.205-11

Depreciation (continued)

- Depreciation is not permitted (**unallowable**) on fully depreciated assets, but a “reasonable charge” is permitted per an advanced agreement
- ASC 840 requires capital leases to be treated as purchased assets to be capitalized and the capitalized value of such assets be distributed over the useful lives as depreciation charges **subject to these limitations**
 - For sale and leaseback, only **allowable up to** the amount it would be allowed if the contractor retained title
 - If the terms of the capital lease pertain to related parties, the depreciation charges **are limited to such charges** if it was with an unrelated party

FAR 31.205-13

Employee Morale, Health, Welfare, Food Service, Dormitory Costs & Credits

- Allowable costs to improve work conditions
 - House publications, health clinics, wellness-fitness centers, employee counseling, food and dormitory services (includes: dining rooms, canteens, lunch wagons, vending machines and living accommodations)
- Gifts to employees are unallowable
- Achievement awards are allowable if in a plan or policy
- Recreational costs unallowable unless for company sponsored sports teams have the goal of improving loyalty, team work or physical fitness

FAR 31.205-14

Entertainment

- All types of entertainment are unallowable
 - Amusements, diversions, social activities, tickets to shows or sporting events, meals, lodging, rentals, transportation or gratuities
 - Memberships in: social, dining, or country clubs or organizations with similar functions
- If unallowable under this section, cannot be made allowable under another cost principle

FAR 31.205-15

Fines, Penalties, Mischarging

- The cost relating to violations of federal, state or local entities is **unallowable**, unless permitted by contract terms (e.g. tax disputes or parking violations)
- Mischarging costs are **unallowable**
 - Covers the cost to ascertain the extent of mischarge, to correct the problem, and re-construct damaged records

FAR 31.205-16

Gains and Losses on Disposition or Impairment of Depreciable Property and Other Capital Assets

- Gains and losses from the sale, retirement, or other disposition of depreciable property shall be included in the year in which they occur as credits or charges to the cost grouping(s) they were assigned
- Generally, the gain or loss is the difference between the net amount realized and the un-depreciated balance of the asset

FAR 31.205-17

Idle Facilities and Idle Capacity Costs

- Costs of idle facilities or idle capacity includes: maintenance, repair, housing, rent, and property taxes, insurance and depreciation
- Idle capacity is less than 100% of unused capacity of partially used facilities
- Idle facility are completely unused facilities in excess of the contractor's current needs

FAR 31.205-17

Idle Facilities and Idle Capacity Costs (continued)

- **Unallowable unless**
 - Necessary to meet fluctuations in workload
 - Necessary when acquired and now idle because of changes in requirements, production economies, reorganization, termination or other costs which could not have reasonably be seen
 - Costs of idle facilities are **allowable** for a reasonable period, ordinarily up to 1 year, depending upon the initiative taken to use, lease, or dispose of the idle facilities
 - Widespread idle capacity may be idle facility

FAR 31.205-18

B&P and IR&D

- Cost principle makes B&P and IR&D **allowable** as indirect cost
- **B&P**
 - Costs of preparing, submitting and supporting bid and proposals
- **IR&D**
 - Project costs for
 - Basic research
 - Applied research
 - Development
 - Systems other than concept formulation studies
 - Dfars \$1.1 million exemption before providing support to Defense Department

FAR 31.205-19

Insurance and Indemnification

- Regardless of whether the contractor is covered by CAS, with respect to self-insurance, it is subject to the following limitations
 - The contractor shall measure, assign and allocate self-insurance costs per CAS 416
 - Contractor must comply with FAR Part 28 insurance program. Compliance with Part 28 does not constitute allowability
 - If purchased insurance is available, any self-insurance charge plus insurance administration expenses in excess of the cost of comparable purchased insurance is unallowable
 - Self-insurance charges for risks of catastrophic losses are **unallowable**

FAR 31.205-19

Insurance and Indemnification (continued)

- Costs of business interruption or other similar insurance shall be limited to exclude coverage or profit
- Limitations on property insurance that exceed the acquisition cost of the insured asset
 - If no formal written policy, the excess of property insurance above its value is **unallowable**
- Insurance for the risk of loss of Government property is **allowable** if the contractor is liable for such loss and other requirements
- Keyman insurance on the lives of corporate officers or owners is **unallowable** if the proceeds are returned to the company
- Cost of insurance to protect the contractor against the cost of correcting its own defects in materials and workmanship are **unallowable**; unless casualty losses resulting from defects in materials or workmanship are **allowable**
- Premiums for retroactive or back-dated insurance to cover losses that already occurred is **unallowable**
- Late premium payment charges related to employee deferred compensation plan insurance incurred per ERISA are **unallowable**

FAR 31.205-20

Interest & Other Financial Costs

- **Unallowable**
 - Interest on borrowings (regardless of form)
 - Costs of financing or re-financing
 - Bond discounts
 - Preparation of a prospectus or stock rights



FAR 31.205-22

Lobbying and Political Activity Costs

- **Unallowable**
 - Attempts to influence outcome of elections
 - Establishing, administering, contributing or paying expenses to a political party, campaign, PAC to influence the outcome of elections
 - Any attempt to influence Federal, state or local legislation or an officer of the Executive branch of the Federal government

FAR 31.205-22

Lobbying and Political Activity Costs (continued)

- **Unallowable**
 - Preparing, distributing or using publicity or propaganda by urging members of the general public or any segment to contribute or participate in mass demonstration, march, rally, fund raising drive, lobbying campaign or letter writing, or telephone campaign (no mention of social media but it applies)
 - Any attempt to influence Federal, state or local legislation or an officer of the Executive branch of the Federal government

FAR 31.205-23

Losses on Other Contracts

- **Unallowable**
 - An excess of costs over income under any other contract (including the contractor's contributed portion under cost-sharing contracts)

FAR 31.205-26

Material Costs

- Materials include the cost of raw materials, parts, sub-assemblies, components and manufactured supplies, whether purchased or manufactured by the contractor
- Material cost include reasonable overruns, spoilage, or defective work
- Adjust the costs of material for income and other credits
 - Including trade discounts, refunds, rebates, cash discounts, credits for scrap, salvage
 - Credit income and other credits directly to material

FAR 31.205-26

Material Costs (continued)

- When materials are purchased specifically for and are identified solely with performance under a contract
- The actual purchase cost of those materials should be charged to the contract
- Materials, supplies and services that are sold or transferred between divisions, subsidiaries or affiliates under common control should be at **cost unless**
 - There is an established practice of the transferring organization to price inter-organizational transfers at **other than cost** for **commercial work**, and
 - The item transferred **qualifies for an exception** [exception to obtaining certified cost or pricing data per FAR 15.403-1] and the contracting officer does not determined **the price to be unreasonable**

FAR 31.205-27

Organization Costs

- **Unallowable**
 - Planning or executing the organization or reorganization of corporate structure of a business
 - Resisting or planning to resist the reorganization of the corporate structure of a business or a change in the controlling interest in the ownership of a business
 - Raising capital (net worth plus long-term liabilities)
 - Unallowable items include: fees for attorneys, accountants, brokers, promoters and organizers, management consultants and investment counselors
 - Unallowable “reorganization” costs include: cost of any change in the contractor’s financial structure resulting in alterations in the rights and interests of security holders

Polling Question #3

What is the biggest concern with consulting cost?

- A. Finding the lowest price consultant*
- B. Finding the highest quality in services*
- C. Retaining the consultant agreement*
- D. Only 1 year of performance is allowable*

FAR 31.205-28

Other Business Expenses

- **Allowable items**
 - Registry and transfer charges resulting from changes in ownership of securities issued by the contractor
 - Cost of shareholder's meetings
 - Normal proxy solicitations
 - Preparing and publishing reports to shareholders
 - Preparing and submitting required reports and forms to taxing and other regulatory bodies
 - Incidental costs of directors' and committee meetings
 - Other similar costs

FAR 31.205-29

Plant Protection Costs

- **Allowable items**
 - Wages, uniforms and equipment of personnel engaged in plant protection
 - Depreciation on plant protection capital assets
 - Necessary expenses to comply with military requirements

FAR 31.205-30

Patent Costs

- **Allowable items as a direct requirement of a Government contract**
 - Costs of preparing invention disclosures, reports, and other documents
 - Costs for searching the art to the extent necessary to make the invention disclosures
 - Other costs in connection with the filing and prosecution of US patent application where title or royalty-free license is to be conveyed to the Government
 - *General counseling services relating to patent matters, such as advice on patent laws, regulations, clauses and employee agreements are allowable*
- **Unallowable patent costs are:** those patent costs not required by the contract are unallowable, except general counseling services

FAR 31.205-32

Pre-Contract Costs

- **Allowable items**
 - Costs incurred before the effective date of the contract directly pursuant to the negotiation and in anticipation of the contract award when such incurrence is necessary to comply with the proposed contract delivery schedule. These costs are allowable to the extent that they would have been allowable if incurred after the date of the contract.

FAR 31.205-33

Professional & Consulting Costs

- **Allowable**
 - Costs of professional and consultant services are allowable subject to some exceptions are reasonable in relation to the services rendered and when not contingent upon recovery of the costs from the Government
- **Unallowable**
 - Services to improperly obtain, distribute, or use information or data protected by law or regulation
 - Services that are intended to improperly influence the contents of solicitations, evaluation of proposals/quotations, or
 - Any services obtained, performed, or otherwise resulting in a violation of any statute or regulation prohibiting improper business practices or conflicts of interest
 - Services performed which are not consistent with the purpose and scope of the services contract

FAR 31.205-33

Professional & Consulting Costs (continued)

- **Allowable**
 - In determining **allowability** of costs (including retainer fees) in a particular case, no single factor or any special combination of factors is necessarily determinative
 - The contracting officer shall consider the following factors
 - The nature and scope of the service rendered in relation to the service required
 - The necessity of contracting for the service, considering the contractor's capability in the particular area
 - The past pattern of acquiring such services and their costs, particularly in the years prior to the award of Government contracts

FAR 31.205-33

Professional & Consulting Costs (continued)

Factors S/B Considered

- The impact of Government contracts on the contractor's business
- Whether the proportion of Government work to the contractor's total business is such as to influence the contractor in favor of incurring the cost, particularly when the services rendered are not of a continuing nature and have little relationship to work under Government contracts
- Whether the service can be performed more economically by employment rather than by contracting
- The qualifications of the individual or concern rendering the service (e.g. description of the service, estimate of time required, rate of compensation, termination provisions)

FAR 31.205-33

Professional & Consulting Costs (continued)

- The actual services performed are *documented* in accordance with *below*
 - Fees for services rendered are allowable only when supported by evidence of the nature and scope of the service furnished
 - Retainer agreements generally are not based on specific statements of work
 - Evidence necessary to determine that work performed is proper and does not violate law or regulation shall include

FAR 31.205-33

Professional & Consulting Costs (continued)

- Details of all agreements (e.g. work requirements, rate of compensation, and nature and amount of other services) with the individuals or organizations providing the services and details of actual services performed
- Invoices or billings submitted by consultants, including sufficient detail as to the time expended and nature of actual services provided
- Consultants' work products and related documents, such as trip reports indicating persons visited and subjects discussed, minutes of meetings and collateral memoranda and reports

FAR 31.205-34

Recruitment Costs

- **Allowable** help-wanted ads, travel for applicants, employment agency costs not in excess of customary costs
- **Unallowable** help-wanted ads
 - Does not describe specific positions or classes or positions, or
 - Includes material that is not relevant for recruitment purposes, such as extensive illustrations or descriptions of the company's products or capabilities

FAR 31.205-35

Relocation Costs

- Cost for assignment of new recruit or re-assigning existing personnel
- There is a list of several types of allowable relocation costs with limits
- (d) **Unallowable Employee Relocation Cost**
 - If relocation costs for an employee has been allowed either as an allocable direct or indirect cost, and the employee resigns within 12 months for reasons within the employee's control, the contractor shall refund or credit the relocation costs to the government

FAR 31.205-36

Rental Costs

- This cost principle pertains to the renting or leasing of real or personal property acquired as “operating leases” per ASC 840
- The following costs are allowable
 - Rental costs under operating lease to the extent the rates were reasonable at the time of the lease decision in considering
 - Rental costs of comparable property
 - Market conditions in this area
 - The type, life expectancy, condition, and value of the property leased
 - Alternatives available
 - Other provisions of the agreement
 - NEW ASC 842 Finance leases

FAR 31.205-36

Rental Costs (continued)

- Rental cost on a SALE & LEASEBACK arrangement only up to the amount the contractor would be allowed if the contractor retained title, computed based on the net book value of the asset on the date the contractor becomes a lessee of the property, adjusted for any gain or loss recognized
- Charges in the nature of rent for property between any divisions, subsidiaries, or organizations under common control, to the extent that they do not exceed the normal costs of ownership, such as depreciation, taxes, insurance, cost of money, and maintenance (excluding interest or other unallowable costs)

FAR 31.205-37

Royalties and Other Costs for Use of Patents

- Royalties on patent or amortization of the cost of purchasing a patent or patent rights necessary for the proper performance on the contract and applicable to contract products or processes are **allowable**
- Care should be exercised in determining reasonableness when the royalties may have been arrived at as a result of less-than-arm's length bargaining
- A patent formerly owned by the contractor, the royalty amount **allowed** should not exceed the cost which would have been allowed had the contractor retained title

FAR 31.205-37

Royalties and Other Costs for Use of Patents (continued)

- **Unallowable** royalties on patent or amortization of a purchased patent when
 - The Government already has a license or the right to free use of the patent
 - The patent is adjudicated to be invalid, or has been administratively determined to be invalid
 - The patent is considered unenforceable
 - The patent has expired

FAR 31.205-38

Selling Costs

- *Selling* is a generic term encompassing all efforts to market or promote product-service
- **Unallowable selling cost**
 - Advertising FAR 31.205-1(b)
 - Public relations (corporate image enhancement) FAR 31.205-1(a)
- **Allowable selling cost**
 - Bid and proposal costs FAR 31.205-18(a)
 - Economic planning cost FAR 31.205-12
 - Long range strategic marketing plans covering economic dislocations or market alterations
 - Market planning FAR 31.205-38(b)
 - Direct selling FAR 31.205-38(c)(1)

FAR 31.205-38

Selling Costs (continued)

Direct selling cost is allowable

- Induce particular customers to purchase particular products or services
- Characterized by person-to-person contact
- Familiarizing a potential customer with:
 - Products or services
 - Conditions of sale
 - Service capabilities
 - Negotiation
 - Liaison between customer and contractor personnel
 - Technical and consulting activities
 - Individual demonstrations
 - Adapt or apply product or services to customer's requirements

FAR 31.205-38

Selling Costs (continued)

Market planning

- Involves market research and analysis and general management planning concerned with development of the contractor's business. Long-range market planning costs are subject to the **allowability** provisions in FAR 31.205-12 (Economic Planning Cost)
- Other market planning costs are **allowable**

FAR 31.205-41

Taxes

- State and local taxes required to be and are paid or accrued in accordance with GAAP are **allowable**.

Fines and penalties are not considered taxes

- **Unallowable** taxes are Federal income and excess profits taxes
- **Unallowable** taxes in connection with financing, refinancing, refunding operations, or reorganizations
- **Unallowable** taxes from which exemptions are available to the contractor directly or available to the contractor based on an exemption afforded the Government

FAR 31.205-41

Taxes (continued)

- **Unallowable** taxes (including excises) on real or personal property or on the value, use possession or sale thereof, which is used solely in connection with work other than on Government contracts
- **Unallowable** tax accruals designed to account for the tax effects of differences between taxable income and pretax income as reflected by the books of account and financial statements
- **Limitation:** taxes on property either Government or non-Government work should be directly applicable to the respective category of work unless amounts involved are insignificant
- **Credits:** Any taxes, interest or penalties that were allowed as contract costs and are refunded to the contractor shall be credited or paid to the Government in the manner it directs

FAR 31.205-42

Termination Costs

- Contract terminations generally give rise to the incurrence of costs or *the need for special treatment of costs that would have not have arisen had the contract not been terminated*. Special cost principles for terminations are provided in this section. See FAR Subpart 49 for Terminations.
 - Common items. Common items reasonably usable on the contractor's other work shall be **unallowable** unless the contractor submits evidence that the items could not be retained without sustaining a loss. Acceptance of common items as **allocable** of such items on hand, in transit, and on order are in excess of the reasonable quantitative requirements of other work.
 - Costs continuing after termination. Despite all reasonable efforts by the contractor, cost which cannot be discontinued immediately after the effective date of the termination are generally **allowable**, unless due to negligence or willful failure of the contractor to discontinue the costs shall be **unallowable**.
 - Initial costs are starting load and preparatory costs are **allowable** with limitations as provided more in detail in this cost principle.

FAR 31.205-42

Termination Costs (continued)

- Contract Loss of useful value of special tooling, and special machinery and equipment is generally **allowable** with limitations as provided more in detail in this cost principle
 - Rentals under unexpired leases less the residual value of such leases are generally **allowable** when shown to have been reasonably necessary for the performance of the contract
 - The contractor must make all reasonable efforts to terminate, assign, settle or otherwise reduce the cost of leases
 - Settlement costs for accounting, legal, clerical and similar support costs reasonably necessary for preparation and presentation, including supporting data, settling of claims to the Termination Contracting Officer
 - Termination and settlement of subcontracts
 - Reasonable costs of storage, transportation, protection and disposition of property acquired or produced for the contract
 - Indirect costs related to salary and wages incurred as settlement expenses
 - Subcontractor claims are generally allowable

FAR 31.205-43

Trade, Business, Technical & Professional Activity Costs

- Memberships and subscriptions to trade, business, technical and professional organizations are **allowable**
- Conventions, symposiums and conferences that have the purpose of disseminating technical, trade, business or professional information is **allowable**
 - Costs to organize, set up, space rental, transportation, subsistence and incidentals
 - Costs of attendance by contractor personnel and their travel

FAR 31.205-44

Training and Education Cost

- Grants to educational or training institutions are considered donations and are **unallowable**
- Training for other than bona-fide employees or for dependents is **unallowable**
- Contractor contributions to college saving plans for employee dependents is **unallowable**
- **Allowable** part-time college level includes: tuition, training materials, textbooks (stated by default)
- **Unallowable** is the cost of salaries attending undergraduate level classes or part-time graduate level classes during work hours
- **Allowable** full-time college education is limited to post graduate and includes salary and subsistence, limited to a max of 2 years

FAR 31.205-46

Travel Costs

- Costs for transportation, lodging, meals and incidental expenses
- Costs incurred by contractor personnel on official company business are **allowable, subject to certain limitations** (details in this cost principle)
- Costs of transportation may be based on mileage rates, actual cost incurred, or a combination thereof, provide the method used results in a reasonable charge
- Costs of lodging, meals and incidental expenses may be based on per diem, actual expenses or a combination thereof, provided the method used results in a reasonable charge

FAR 31.205-46

Travel Costs (continued)

- Costs for Lodging, meals and incidentals are reasonable if
 - Allowable to the extent such expenses do not exceed the daily per diem rates permitted at the time of travel
 - FTR under GSA, 48 contiguous states
 - JTR, Alaska, Hawaii, Puerto Rico
 - Dept. of State, Non-US locations
 - Exceptions to JTR/FTR are very rare
 - All of these items have to be met to get an exception:
 - Actual expenses exceed a JTR/FTR per diem up to the higher amounts authorized by the Federal civilian employees
 - Sufficient documentation to support higher per diem
 - Internal authorization by government official, or
 - Obtain an advance agreement from the ACO
 - A reduction for part-day travel is required; under GSA per diems 75% of M&IE

FAR 31.205-46

Travel Costs (continued)

- Airfare costs in excess of the lowest priced airfare available to the contractor during normal business hours are unallowable except when such accommodations require circuitous routing, require travel during unreasonable hours, excessively prolong travel
- However, excessive airfare costs must be documented and justified
- Special rules and details in this cost principle pertaining to the cost of travel by contractor-owned or leased or chartered aircraft
- Cost of company-furnished autos that relates to personal use by employees is compensation for personal services and is **unallowable**

FAR 31.205-49

Goodwill Costs

- Good will is an intangible asset which is derived from the “purchase method” of accounting for a business combination when the price paid by the acquiring company exceeds the sum of the identifiable assets acquired less liabilities
- Any method for amortizing the expense or write-off/down of goodwill is unallowable

FAR 31.205-51

Costs of Alcoholic Beverages

- Cost of alcoholic beverages must be segregated as an unallowable cost



FAR 31.205-52

Combinations

- For tangible capital assets, when the “purchase method” of accounting is used whether or not the contract or subcontract is subject to CAS, the allowable depreciation and cost of money shall be based on the capitalized asset values measured and assigned in accordance with CAS 404-50(d), if allocable, reasonable and not otherwise unallowable
- For intangible capital assets, when the “purchase method” of accounting is used, allowable amortization of the cost of money is limited to the total of the amounts that would have been allowed had the combination not taken place

Questions



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